

Capital Gains and Losses and Built-in Gains

1998

Attach this Schedule to your Hawaii S Corporation Income Tax Return — Form N-35

Name	Federal Employer's I.D. No.
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PART I — Short-Term Capital Gains and Losses — Assets Held One Year or Less

a. Kind of property and description (Example: 100 shares of "Z" Co.)	b. Date acquired (mo., day, yr.)	c. Date sold (mo., day, yr.)	d. Gross sales price	e. Cost or other basis, plus expense of sales	f. Gain or (loss) (d minus e)	g. Gain or (loss) Attributable to Hawaii
1						
2 Short-term capital gain from installment sales. (from federal Form 6252).					2	
3 Short-term capital gain or (loss) from like-kind exchanges. (from federal Form 8824).					3	
4 Add lines 1, 2, and 3. Enter here.					4	
5 Tax on short term gain included on line 27 below. (Enter same amount in cols. f and g)					5	
6 Net short-term capital gain or (loss). Line 4 minus line 5. Enter this amount here and on Form N-35, Schedule K, line 4d or line 6.					6	

PART II — Long-Term Capital Gains and Losses — Assets Held More Than One Year

7						
8 Long-term capital gain from installment sales. (from federal Form 6252).					8	
9 Long-term capital gain or (loss) from like-kind exchanges. (from federal Form 8824)					9	
10 Add lines 7, 8, and 9. Enter here.					10	
11 Tax on long-term gain included on lines 21 and 27 below. (Enter same amount in cols. f and g)					11	
12 Net long-term capital gain or (loss). Line 10 minus line 11. Enter this amount here and on Form N-35, Schedule K, line 4e or line 6.					12	

PART III — Capital Gains Tax (See Instructions before completing this part.)

13 Enter IRC section 1231 gain from Schedule D-1.	13	
14 Net long-term capital gain or (loss). (add lines 10 and 13)	14	
Note: If the corporation is liable for the excess net passive income tax (line 22a, page 1, Form N-35), or the built-in gains tax (Part IV below), see Instructions before completing line 15.		
15 Net capital gain — Enter excess of net long-term gain (line 14, column g) over net short-term capital loss (line 4, column g).	15	
16 Statutory minimum.	16	\$25,000
17 Line 15 minus line 16.	17	
18 Enter 6.4% of line 17.	18	
19 Taxable income. (see Instructions and attach computation schedule)	19	
20 Enter tax on line 19 amount. (see Instructions for computation of tax)	20	
21 Tax — Enter smaller of line 18 or line 20.	21	

PART IV — Built-in Gains Tax (See Instructions before completing this part.)

22 Excess of recognized built-in gains over recognized built-in losses. (see Instructions and attach computation schedule).	22	
23 Taxable income. (see Instructions and attach computation schedule)	23	
24 Net recognized built-in gain—Enter smaller of line 22 or line 23. (see Instructions)	24	
25 IRC section 1374(b)(2) deduction.	25	
26 Subtract line 25 from line 24. (If zero or less, enter zero here and on line 27)	26	
27 Tax — Enter 6.4% of line 26.	27	
28 Line 21 plus line 27. Enter here and on Form N-35, page 1, line 22b.	28	

INSTRUCTIONS

Section references are to the Internal Revenue Code, unless otherwise noted.

Purpose of Schedule

Schedule D (Form N-35) is used by S corporations to report sales or exchanges of capital assets and gains on distributions to shareholders of appreciated assets that are capital assets (hereafter referred to as distributions). In addition, this schedule is intended to partition the "flow-through" of an S corporation's net capital gain to its shareholders and to attribute the gain applicable to Hawaii sources. It will directly assist the shareholders of the corporation in properly reporting such gains for the period.

If the corporation elected to be a Hawaii S corporation before 1987 (or made the election during 1987 or 1988 and qualifies for the transitional relief from the built-in gains tax), and had net capital gain (line 9) of more than \$25,000, it may be liable for a capital gains tax on the gain in excess of \$25,000. The tax is figured in Part III of Schedule D.

Generally, if the corporation elected Hawaii S corporation status after 1986, was a C corporation at the time it made the election, and has net recognized built-in gain as defined in section 1374(d)(2) on assets attributable to Hawaii, it is liable for the built-in gains tax. Assets are attributable to Hawaii if they are physically located in Hawaii, are used in a Hawaii business, or if, in the case of intangible assets, the S corporation has its commercial domicile in Hawaii. The tax is figured in Part IV of Schedule D. Sales, exchanges, and distributions of property other than capital assets, including property used in a trade or business, involuntary conversions (other than casualties or thefts), and gain from the disposition of an interest in oil, gas, or geothermal property should be reported on Schedule D-1, Sales of Business Property, see the instructions for Schedule D-1. If property is involuntarily converted because of a casualty or theft, use federal Form 4684, Casualties and Thefts.

Parts I and II

Generally, report sales and exchanges (including like-kind exchanges) even if there is no gain or loss. In Part I, report the sale, exchange, or distribution of capital assets held one year or less. In Part II, report the sale, exchange, or distribution of capital assets held more than 1 year. Use the trade dates for the dates of acquisition and sale of stocks and bonds on an exchange or over-the-counter market.

For more information, see federal Publication 544, Sales and Other Dispositions of Assets, and federal Publication 589, Tax Information on S Corporations.

Exchange of like-kind property.—Complete and attach federal Form 8824, Like-Kind Exchanges, to the corporation's return for each exchange. Also, report the exchange of like-kind property on Schedule D or on Schedule D-1, whichever applies. Report it even if no gain or loss is recognized when business or investment property is exchanged for property of like-kind. For exceptions, see federal Publication 544.

Enter the gain or loss from federal Form 8824 in column (f) and in column (g) if the property traded was Hawaii property. Write in the top margin of Schedule D "Like-Kind Exchange" or if the exchange involved a related party, write "Related Party Like-Kind Exchange."

Special Rules for the Treatment of Certain Gains and Losses

See the instructions for federal Schedule D (Form 1120S) for a discussion of special rules for the treatment of certain gains and losses.

How to Determine the Cost or Other Basis of the Property

See the instructions for federal Schedule D (Form 1120S) for a discussion on how to determine the cost or other basis of the property.

Part III—Capital Gains Tax

If the net long-term capital gain attributable to Hawaii assets is more than the net short-term capital loss attributable to Hawaii assets, there is a net capital gain attributable to Hawaii assets (net capital gain). If this gain exceeds \$25,000 and the corporation elected to be a Hawaii S corporation before 1987 (or made the election during 1987 or 1988 and qualifies for the transitional relief from the built-in gains tax), the corporation may be liable for income tax on the gain.

By answering the following questions, it can be determined whether the corporation is liable for the tax. If answers to questions A, B, and C are "Yes," the tax applies and Part III of Schedule D must be completed. Otherwise, the corporation is not liable for the tax.

If net capital gain is more than \$25,000 and the corporation is not liable for the tax, answer questions A through C below as an explanation of why it is not liable for the tax.

- A.** Is net capital gain (line 15, Schedule D (Form N-35)) more than \$25,000 and more than 50% of taxable income (line 19, Schedule D (Form N-35))? ☐ Yes ☐ No
- B.** Is taxable income (line 19, Schedule D (Form N-35)) more than \$25,000? ☐ Yes ☐ No
- C.** Does any long-term capital gain (line 14, Schedule D (Form N-35)) represent gain from substituted basis property (defined below)? ☐ Yes ☐ No

For purposes of the capital gains tax, **substituted basis property** is property that:

1. Was acquired by the S corporation during the period that began 36 months before the first day of the tax year and ended on the last day of the tax year, and

2. Has a basis determined by reference to the basis of any property in the hands of another corporation, if the other corporation was **not** an S corporation throughout the period that began the later of:

- a.** 36 months before the first day of the tax year, or
- b.** The time the other corporation came into existence,

and ended on the date the other corporation transferred the property used to determine the basis of the property acquired by the S corporation.

If the answer to question C is "Yes" and the tax is applicable, multiply the net capital gain from property described in question C (reduced by any excess net passive income attributable to this gain—see instruction for line 15) by 6.4%. If this amount is less than the tax figured on line 20, enter this amount on line 21 and write to the right of the amount, "Substituted basis." Attach the computation of the substituted basis amount to Schedule D. (See section 1374(c)(3) as in effect before the enactment of the Tax Reform Act of 1986.)

Line 15—If the corporation is liable for the tax on excess net passive income (Form N-35, page 1, line 22a) or the built-in gains tax and capital gain or loss was included in the computation of either tax, figure the amount to enter on line 15 as follows:

Step 1—Refigure lines 1, 2, and 7 through 13 of Schedule D by:

- (a)** excluding the portion of any recognized built-in capital gain or loss that does not qualify for transitional relief, and
- (b)** reducing any capital gain taken into account in determining passive investment income by the

portion of excess net passive income attributable to such gain. The portion so attributable is figured by multiplying excess net passive income by a fraction, the numerator of which is the amount of the capital gain (less any expenses attributable to such gain), and the denominator of which is net passive income.

Step 2—Refigure lines 6, 14, and 15 of Schedule D using the amounts determined in Step 1.

Line 19—Figure taxable income by completing lines 1 through 10 and 1 through 12 of Schedule J of Form N-30, Hawaii Corporation Income Tax Return. Enter the amount from Schedule J, line 12 that is attributable to Hawaii on line 19 of Schedule D. Attach to Schedule D the Form N-30 computation or other worksheet used to figure taxable income.

Line 20—Figure the corporate income tax based on the taxable income on line 19 as if the S corporation were a C corporation and enter the tax on line 20. You may use Schedule J of Form N-30 to make your computation. Attach your tax computation to Schedule D.

Part IV—Built-In Gains Tax

Section 1374 provides for a tax on built-in gains that applies to certain corporations that made the election to be an S corporation after 1986. This tax does not apply to any corporation that has been an S corporation for each of its tax years, unless the corporation acquired an asset with a basis determined by reference to its basis (or the basis of any other property) in the hands of a C corporation.

Transitional Relief from Built-In Gains Tax

See the instructions for federal Schedule D (Form 1120S) for a discussion of special transitional relief from the built-in gains tax for qualified corporations.

Line 22—Enter the amount that would be the taxable income of the corporation for the tax year if only recognized built-in gains (including any carryover of gain under section 1374(d)(2)(B)) attributable to Hawaii and recognized built-in losses attributable to Hawaii were taken into account.

See the instructions for federal Schedule D (Form 1120S) for definitions of recognized built-in gain and recognized built-in loss.

A qualified corporation must show on an attachment to Schedule D its total net recognized built-in gain attributable to Hawaii and also list separately the gain or loss attributable to Hawaii that is: (1) gain or loss from capital assets held 6 months or less and (2) gain or loss from assets for which the disposition results in ordinary income or loss. A nonqualified corporation must show on an attachment its total net recognized built-in gain attributable to Hawaii and list separately any capital gain or loss and ordinary gain or loss.

Line 23—See the instructions for line 19. Enter the amount computed on line 23.

Line 24—Do not enter on line 24 more than the excess (if any) of the net unrealized built-in gain attributable to Hawaii over the net recognized built-in gain attributable to Hawaii for prior years. This is the amount that should have been entered in item 11 on Form N-35, page 2. See section 1374(c)(2). If, for any tax year, the amount on line 22 exceeds the taxable income on line 23, the excess is treated as a recognized built-in gain attributable to Hawaii in the succeeding tax year. This carryover provision applies only in the case of an S corporation that made its election to be an S corporation on or after March 31, 1988. See section 1374(d)(2)(B).

Line 25—Enter the section 1374(b)(2) deduction. Generally, this is any net operating loss carryforward attributable to Hawaii or capital loss carryforward (to the extent of net capital gain included in recognized built-in gain for the tax year) attributable to Hawaii arising in tax years for which the corporation was a C corporation. For details, see section 1374(b)(2).